

(4) At the conclusion of the on-site portion of the review process, the Departments reviewers shall hold an exit conference with facility representatives. Reviewers will share written findings for reviewed records.

41.23.4 Sanctions

The Department shall compute the quarterly facility average case mix index, as described in Section 80.3 of these principles. Effective with assessment reviews on or after October 1, 2000, the following sanctions shall be applied to the allowable case mix adjusted direct care cost component for the subsequent quarter for all Medicaid residents of the facility, for which the following assessment review error rates are determined. Such sanctions shall be a percentage of the total direct care rate after the application of the case mix adjustments and upper limit.

- (1) A 2% decrease in the total direct care cost component will be imposed when the NF assessment review results in an error rate of 34% or greater, but is less than 37%.
- (2) A 5% decrease in the total direct care cost component will be imposed when the NF assessment review results in an error rate of 37% or greater, but is less than 41%.
- (3) A 7% decrease in the total direct care cost component will be imposed when NF assessment review results in an error rate of 41% or greater, but is less than 45%.
- (4) A 10% decrease in the total direct care cost component will be imposed when the NF assessment review results in an error rate of 45% or greater.

41.23.5 Failure to complete MDS corrections by the nursing facility staff within 7 days of a written request by staff of the Bureau of Medical Services may result in the imposition of the deficiency per diem as specified in Principle 152 of these Principles of Reimbursement. Completed MDS corrections and assessments, as defined in Section 41.2, shall be submitted to the Department or its designee according to HCFA guidelines.

41.23.6 Appeal Procedures: A facility may administratively appeal a Bureau of Medical Services rate determination for the direct care cost component. An administrative appeal will proceed in the following manner:

- (1) Within 30 days of receipt of rate determination, the facility must request, in writing, an informal review before the Director of the Bureau of Medical Services or his/her designee. The facility must forward, with the request, any and all specific information it has relative to the issues in dispute. Only issues presented in this manner and time frame will be considered at an informal review or at a subsequent administrative hearing.
- (2) The Director of his/her designee shall notify the facility in writing of the decision made as a result of the informal review. If the facility disagrees with the results of the informal review, the facility may request an administrative hearing before the Commissioner or a presiding officer

designated by the Commissioner. Only issues presented in the informal review will be considered at the administrative hearing. A request for an administrative hearing must be made, in writing, within 30 days of receipt of the decision made as a result of the informal review.

(3) To the extent the Department rules in favor of the facility, the rate will be corrected.

(4) To the extent the Department upholds the original determination of the Bureau of Medical Services, review of the results of the administrative hearing is available in conformity with the Administrative Procedures Act, 5 M.R.S.A. §11001 et seq.

41.3 Allowable costs for the Direct Care component of the rate shall include:

41.31 Direct Care Cost. The base year costs for direct care shall be the actual audited direct care costs incurred by the facility in the fiscal year ending in calendar year 1998 except for facilities whose Medicaid rates are based on proforma cost reports in accordance with Sections 80.6 and 80.7. All base year costs are subject to upper limits defined in Section 80.3.3.5.

43 ROUTINE COST COMPONENT

All allowable costs not specified for inclusion in another cost category pursuant to these rules shall be included in the Routine cost component subject to the limitations set forth in these Principles. The base year costs for the routine cost component shall be the audited costs incurred by the facility in the fiscal year ending in calendar year 1998, except for facilities whose Medicaid rates are based on proforma cost reports in accordance with Sections 80.6 and 80.7. All base year costs are subject to upper limits defined in Section 80.5.4.

43.1 Principle. All expenses which providers must incur to meet state licensing and federal certification standards are allowable.

43.2 All inventory items used in the provision of routine services to residents are required to be expensed in the year used. Inventory items shall include, but are not limited to: linen and disposable items.

43.3 Allowable costs shall also include all items of expense efficient and economical providers incur for the provision of routine services. Routine services mean the regular room, dietary services, and the use of equipment and facilities.

43.4 Allowable costs for the Routine component of the rate shall include but not be limited to costs reported in the following functional cost centers on the facility's cost report.

- (a) fiscal services, (not to include accounting fees)
- (b) administrative services and professional fees not to exceed the administrative and management ceiling,
- (c) plant operation and maintenance including utilities,
- (d) laundry and linen,
- (e) housekeeping,

- (f) medical records,
- (g) subscriptions related to resident care,
- (h) employee education, as defined in Section 43.42.9, except wages related to initial and on-going nurse aide training as required by OBRA,
- (i) dietary,
- (j) motor vehicle operating expenses,
- (k) clerical,
- (l) transportation, (excluding depreciation),
- (m) office supplies/telephone,
- (n) conventions and meetings within the state of Maine,
- (o) EDP bookkeeping/payroll,
- (p) fringe benefits, to include:
 - (1) payroll taxes,
 - (2) qualified retirement plan contributions,
 - (3) group health, dental, and life insurance, and
 - (4) cafeteria plans.
- (q) payroll taxes,
- (r) one association dues, the portion of which is not related to lobbying
- (s) food, vitamins and food supplements,
- (t) director of nursing, and fringe benefits,
- (u) social services, and fringe benefits,
- (v) pharmacy consultant, dietary consultant, and medical director.

See the explanations in Section 43.42.1 - 43.45 for a more complete description of allowable costs in each cost center.

43.42.1 Allowable Administration and Management Expenses.

43.42.11 Principle. A ceiling shall be placed on reimbursement for all compensation for administration and policy making functions and all expenses incurred for management and financial consultation, including accounting fees that are incurred by a related organization or the facility's operating company. Any compensation received by the individual who is listed as the administrator on the facility's license for any other services such as nursing, cooking, maintenance, bookkeeping and the like shall also be included within this ceiling.

This ceiling shall be increased quarterly by the inflationary factor as defined in Section 91 to reflect the rate of inflation from July 1, 1995 to the appropriate quarter. To establish the prospective rate for nursing facilities the administrative ceiling in effect at the beginning of a facility's fiscal year will apply to the entire fiscal year of that facility.

43.42.12 For fiscal years beginning on or after July 1, 1995, the statewide average professional accounting costs by bed size (0-30, 31-50, 51-100, over 100) will be included in the administrative and policy - planning ceiling. Only those reasonable, necessary and proper accounting costs which

are appropriate to the operation of nursing facilities are considered allowable accounting costs and will be included in the determination of the state wide average.

43.42.2 Ceiling. The administration and policy-planning ceiling that is in effect as of July 1, 1995 is listed below. The ceiling shall be increased quarterly to reflect the rate of inflation from July 1, 1995, to the appropriate quarter.

*up to 30 beds: \$37,772 plus \$637 for each licensed bed in excess of 10;

*31 to 50 beds: \$54,240 plus \$545 for each licensed bed in excess of 30;

*51 to 100 beds: \$67,432 plus \$364 for each licensed be in excess of 50; and

*over 100 beds: \$90,757 plus \$273 for each licensed bed in excess of 100.

In the case of an individual designated as administrator in more than one (1) facility, the Department shall combine the number of beds in these facilities and apply one hundred and twenty percent (120%) of the above schedule. The total allowance will be prorated to each facility based on the ratio of the facility's number of beds to the combined number of beds for all facilities under the direction of the administrator.

43.42.3 Administration Functions. The administration functions include those duties which are necessary to the general supervision and direction of the current operations of the facility, including, but not limited to, the following:

43.42.3.1 Central Office operational costs for business managers, controllers, reimbursement managers, office managers, personnel directors and purchasing agents are to be included in the administrative and policy-planning ceiling according to an allocation of those costs on the basis of all licensed beds operated by the parent company.

43.42.3.2 Policy Planning Function. The policy planning function includes the policy-making, planning and decision-making activities necessary for the general and long-term management of the affairs of the facility, including, but not limited to the following:

- a) financial management, including accounting fees
- b) establishment of personnel policies
- c) planning of resident admission policies
- d) planning of expansion and financing

43.42.3.3 This ceiling is not to include any Director of Nursing, Dietary Supervisor, or other department head, whose prime duties are not of an administrative nature but who may be responsible for hiring or purchasing for their Department.

43.42.3.4 All other regulations specific to administrative functions in Nursing Facilities that are included in State Licensing Regulations and all other State and Federal regulations.

43.42.4 Dividends and Bonuses. Bonuses, dividends, or accruals for the express purpose of giving additional funds to the administrator or owners of the facility, whether or not they are part of the administrative and management ceiling, will not be recognized as allowable costs by the Department.

43.42.5 Management fees. Management fees charged by a parent company or by an unrelated organization or individual are not allowable costs and are not considered part of the administrative and management ceiling.

43.42.6 Corporate Officers and Directors. Salaries paid to corporate officers and directors are not allowable costs unless they are paid for direct services provided to the facility such as those provided by an administrator or other position required by licensing regulations and included in the staffing pattern which are necessary for that facility's operation.

43.42.7 Central Office Operational Costs. Central office bookkeeping costs and related clerical functions that are not included in the administration and policy-planning ceiling may be allocated to each facility on the basis of total resident census limited to the reasonable cost of bookkeeping services if they were performed by the individual facility.

43.42.7.1 All other central office operational costs other than those listed above in this principle are considered unallowable costs.

43.42.8 Laundry services including personal clothing for Medicaid residents.

43.42.9 Cost of Educational Activities

43.42.9.1 Principle. An appropriate part of the net cost of educational activities is an allowable cost. Appropriate part means the net cost of the activity apportioned in accordance with the methods set forth in these Principles. Expenses for education activities may be evaluated as to appropriateness, quality and cost and may or may not be included as an allowable cost based on the findings.

43.42.9.2 Orientation, On-the-Job Training, In-Service Education and Similar Work Learning. Orientation, on-the-job training, in-service education and similar work learning programs are not within the scope of this principle but, if provided by a staff person, are recognized as normal operating costs for routine services in accordance with the principles relating thereto.

43.42.9.3 Basic Education. Educational training programs which a staff member must successfully complete in order to qualify for a position or a job shall be considered basic education. Costs related to this education are not within the scope of reimbursement.

43.42.9.4 Educational Activities. Educational activities mean formally organized or planned workshops, seminars, or programs of study usually engaged in by the staff members of a facility in order to enhance the quality of resident care within the facility. These continuing education

activities are distinguished from and do not include orientation, basic education programs, on-the-job training, in-service education and similar work learning programs.

43.42.10 Net Cost. The net cost means the cost of an activity less any reimbursement for them from grants, tuition and specific donations. These costs may include: transportation (mileage), registration fees, salary of the staff member if replaced, and meals and lodging as appropriate.

43.43 Motor Vehicle Allowance. Cost of operation of one motor vehicle necessary to meet the facility needs is an allowable cost less the portion of usage of that vehicle that is considered personal. A log which clearly documents that portion of the automobiles use for business purposes is required. Prior approval from the Division of Audit is required if additional vehicles are needed by the nursing facility.

43.44 Dues are allowed only if the nursing facility is able to provide auditable data that demonstrates what portion of the dues is not used for lobbying efforts by the agency receiving the dues payments.

43.45 Consultant Services. The following types of consultative services will be considered as part of the allowable routine costs and be built into the base year routine cost component subject to the limitations outlined in subsections 43.45.1 – 43.45.3.

43.45.1 Pharmacist Consultants

Pharmacist consultant fees paid directly by the facility in the base year, will be included in the routine cost component. In addition to any pharmacist consultant fees included in the base year rate, up to \$2.50 per month per resident shall be allowed for drug regimen review.

43.45.2 Dietary Consultants

Dietary Consultants, who are professionally qualified, may be employed by the facility or by the Department. The allowable amounts paid by the nursing facility to Dietary Consultants in the base year, when reasonable and non-duplicative of current staffing patterns, will be included in the routine cost component.

43.45.3 Medical Directors

The base year cost of a Medical Director, who is responsible for implementation of resident care in the facility, is an allowable cost. The base year allowable cost will be established and limited to \$1,200.

43.5 Principle. Research Costs are not includable as allowable costs.

43.6 Grants, Gifts, and Income from Endowments

43.61 Principle. Unrestricted grants, gifts and income from endowments should not be deducted from operating costs in computing reimbursable costs. However, unrestricted Federal or State grants or gifts received by a facility will be used to reduce the operating costs of that facility. Grants, gifts, or endowment

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income designated by a donor for paying specific operating costs should be deducted from the operating costs or group of costs.

43.61.1 Unrestricted grants, gifts, income from endowment. Unrestricted grants, gifts, and income from endowments are funds, cash or otherwise, given to a provider without restriction by the donor as to their use.

43.61.2 Designated or restricted grants, gifts and income from endowments. Designated or restricted grants, gifts and income from endowments are funds, cash or otherwise, which must be used only for the specific purpose designated by the donor. This does not refer to grants, gifts or income from endowments which have been restricted for a specific purpose by the provider.

43.62 Donations of Produce or Other Supplies. Donations of produce or supplies are restricted gifts. The provider may not impute a cost for the value of such donations and include the imputed cost in allowable costs. If an imputed cost for the value of the donation has been included in the provider's costs, the amount included is deleted in determining allowable costs.

43.63 Donation of Use of Space. A provider may receive a donation of the use of space owned by another organization. In such case, the provider may not impute a cost for the value of the use for the space and include the imputed cost in allowable costs. If an imputed cost for the value of the donation has been included in the provider's cost, the amount included is deleted in determining allowable costs.

43.7 Purchase Discounts and Allowances and Refunds of Expenses.

43.71 Principle. Discounts and allowances received on purchases of goods or services are reductions of the costs to which they relate. Similarly, refunds of previous expense payments are reductions of the related expense.

43.71.1 Discounts. Discounts, in general, are reductions granted for the settlement of debts.

43.71.2 Allowances. Allowances are deductions granted for damages, delay, shortage, imperfections, or other causes, excluding discounts and returns.

43.71.3 Refunds. Refunds are amounts paid back or a credit allowed on account of an over-collection.

43.72 Reduction of Costs. All discounts, allowances, and refunds of expenses are reductions in the cost of goods or services purchased and are not income. When they are received in the same accounting period in which the purchases were made or expenses were incurred, they will reduce the purchases or expenses of that period. However, when they are received in a later accounting period, they will reduce the comparable purchases or expenses in the period in which they are received.

43.73 Application of Discounts Purchase discounts have been classified as cash, trade, or quantity discounts. Cash discounts are reductions granted for the settlement of debts before they are due. Trade discounts are reductions from list prices granted to a class of customers before consideration of credit

terms. Quantity discounts are reductions from list prices granted because of the size of individual or aggregate purchase transactions. Whatever the classification of purchase discounts, like treatment in reducing allowable costs is required. In the past, purchase discounts were considered as financial management income. However, modern accounting theory holds that income is not derived from a purchase, but rather from a sale or an exchange, and the purchase discounts are reductions in the cost of whatever was purchased. The true cost of the goods or services is the net amount actually paid for them. Treating purchase discounts as income would result in an overstatement of costs to the extent of the discount.

43.74 All discounts, allowances, and rebates received from the purchases of goods or services and refunds of previous expense payments are clearly reductions in costs and must be reflected in the determination of allowable costs. This treatment is equitable and is in accord with that generally followed by other governmental programs and third-party organizations paying on the basis of costs.

43.8 Principle. Advertising Expenses. The reasonable and necessary expense of newspaper or other public media advertisements for the purpose of securing necessary employees is an allowable cost. No other advertising expenses are allowed.

43.9 Legal Fees. Legal fees to be allowable costs must be directly related to resident care. Fees paid to the attorneys for representation against the Department of Human Services are not allowable costs. Retainers paid to lawyers are not allowable costs. Legal fees paid for organizational expenses, are to be amortized over a 60 month period.

43.10 Costs Attributable to Asset Sales. Costs attributable to the negotiation or settlement of a sale or purchase of any capital asset (by acquisition or merger) are not allowable costs. Included among such unallowable costs are: legal fees, accounting and administrative costs, appraisal fees, costs of preparing a certificate of need, banking and broker fees, good will or other intangibles, travel costs and the costs of feasibility studies.

43.11 Bad debts, charity, and courtesy allowances are deductions from revenue and are not to be included in allowable cost.

44 FIXED COSTS COMPONENT

44.1 All allowable costs not specified for inclusion in another cost category pursuant to these rules shall be included in the Fixed Cost component subject to the limitations set forth in these Principles. The base year costs for the fixed cost component shall be the costs incurred by the facility in the most recently audited fiscal year. Fixed Costs include:

- 44.1.1 depreciation on buildings, fixed and movable equipment and motor vehicles,
- 44.1.2 depreciation on land improvements and amortization of leasehold improvements,
- 44.1.3 real estate and personal property taxes,
- 44.1.4 real estate insurance, including liability and fire insurance,
- 44.1.5 interest on long term debt,
- 44.1.6 return on equity capital for proprietary providers,

- 44.1.7 rental expenses,
- 44.1.8 amortization of finance costs,
- 44.1.9 amortization of start-up costs and organizational costs,
- 44.1.10 motor vehicle insurance,
- 44.1.11 facility's liability insurance, including malpractice costs and workers compensation,
- 44.1.12 administrator in training,
- 44.1.13 water & sewer fees necessary for the initial connection to a sewer system/water system,
- 44.1.14 portion of the acquisition cost for the rights to a nursing facility license,
- 44.1.15 return on net assets for nonprofit providers.

See the explanations in Sections 44.2 - 44.12 for a more complete description of allowable costs in each of these cost centers.

44.2 Principle. An appropriate allowance for depreciation on buildings and equipment is an allowable cost. The depreciation must be:

44.2.1 Depreciation. Allowance for Depreciation Based on Asset Costs.

44.2.2 Identified and recorded in the provider's accounting records.

44.2.3 Based on historical cost and prorated over the estimated useful life of the asset using the straight-line method.

44.2.4 The total historical cost of a building constructed or purchased becomes the basis for the straight-line depreciation method. Component depreciation is not allowed except on those items listed below with their minimum useful lives:

Electric Components	20 years
Plumbing and Heating Components	25 years
Central Air Conditioning Unit	15 years
Elevator	20 years
Escalator	20 years
Central Vacuum Cleaning System	15 years
Generator	20 years

44.22 Any provider using the component depreciation method that has been audited and accepted for cost reporting purposes prior to April 1, 1980, will be allowed to continue using this depreciation mechanism.

44.23 Where an asset that has been used or depreciated under the program is donated to a provider, or where a provider acquires such assets through testate or intestate distribution, (e.g., a widow inherits a nursing facility upon the death of her husband and becomes a newly certified provider;) the basis of

depreciation for the asset is the lesser of the fair market value, or the net book value of the asset in the hands of the owner last participating in the program. The basis of depreciation shall be determined as of the date of donation or the date of death, whichever is applicable.

44.24 Special Reimbursement Provisions for Energy Efficient Improvements

44.24.1 For the Energy Efficient Improvements listed below which are made to existing facilities, depreciation will be allowed based on a useful life equal to the higher of the term of the loan received (only if the acquisition is financed) or the period by the limitations listed below:

CAPITAL EXPENDITURE

Up to \$5,000.00 - Minimum depreciable period 3 years

From \$5001.00-\$10,000.00 - Minimum depreciable period 5 years

\$10,000.00 and over - Minimum depreciable period 7 years

44.24.2 The above limitations are minima and if a loan is obtained for a period of time in excess of these minima the depreciable period becomes the length of the loan, provided that in no case shall the depreciable period exceed the useful life as spelled out in the American Hospital Association's "Estimated Useful Lives of Depreciable Hospital Assets".

44.24.3 If the total expenditures exceeds \$25,000.00, then prior approval for such an expenditure must be received in writing from the Department. A request for prior approval will be evaluated by the Department on the basis of whether such a large expenditure would decrease the actual energy costs to such an extent as render this expenditure reasonable. The age and condition of the facility requesting approval will also be considered in determining whether or not such an expenditure would be approvable.

44.24.4 The reasonable Energy Efficient Improvements are listed below:

1. Insulation (fiberglass, cellulose, etc.)
2. Energy Efficient Windows or Doors for the outside of the facility, including insulating shades and shutters.
3. Caulking or Weather stripping for windows or doors for the outside of the facility.
4. Fans specially designed for circulation of heat inside the building.
5. Wood and Coal burning furnaces or boilers (not fireplaces).
6. Furnace Replacement burners that reduce the amount of fuel used.
7. Enetrol or other devices connected to furnaces to control heat usage.
8. A Device or Capital Expenditures for modifying an existing furnace that reduces the consumption of fuel.
9. Solar active systems for water and space heating.

10. Retrofitting structures for the purpose of creating or enhancing passive solar gain, if prior approved by the Department regardless of amount of expenditure. A request for prior approval will be evaluated by the Department on the basis of whether energy costs would be decreased to such an extent as to render the expenditure reasonable. The age and condition of the facility requesting approval will be also considered.

11. Any other energy saving devices that might qualify as Energy Efficient other than those listed above must be prior approved by the Department for this Special Reimbursement provision. The Department will evaluate a request for prior approval under recommendations from the Division of Energy Programs on what other items will qualify as an energy efficient device and that the energy savings device is a reliable product and the device would decrease the energy costs of the facility making the expenditure reasonable in nature.

44.24.5 In the event of a sale of the facility the principle payments as listed above will be recaptured in lieu of depreciation.

44.25 Recording of depreciation. Appropriate recording of depreciation encompasses the identification of the depreciable assets in use, the assets' historical costs, the method of depreciation, estimated useful lives, and the assets' accumulated depreciation. The American Hospital Association's "Estimated Useful Lives of Depreciable Hospital Assets" 1983 edition is to be used as a guide for the estimation of the useful life of assets.

44.25.1 For new buildings constructed after April 1, 1980 the minimum useful life to be assigned is listed below:

Wood Frame, Wood Exterior	30 years
Wood Frame, Masonry Exterior	35 years
Steel Frame, or Reinforced Concrete Masonry Exterior	40 years

If a mortgage obtained on the property exceeds the minimum life as listed above, then the terms of the mortgage will be used as the minimum useful life.

44.25.2 For facilities providing two levels of care the allocation method to be used for allocating the interest, depreciation, property tax, and insurance will be based on the actual square footage utilized in each level of care. However, when new construction occurs that is added on to an existing facility the complete allocation based on square footage will not be used. Discrete costing will be used to determine the cost of the portion of the building used for each level of care and related fixed cost will be allocated on the basis of that cost.

44.26 Depreciation method. Proration of the cost of an asset over its useful life is allowed on the straight-line method.

44.27 Funding of depreciation. Although funding of depreciation is not required, it is strongly recommended that providers use this mechanism as a means of conserving funds for replacement of

depreciation assets, and coordinate their planning of capital expenditures with area wide planning of activities of community and state agencies. As an incentive for funding, investment income on funded depreciation will not be treated as a reduction of allowable interest expense.

44.28 Replacement reserves. Some lending institutions require funds to be set aside periodically for replacement of fixed assets. The periodic amounts set aside for this purpose are not allowable costs in the period expended, but will be allowed when withdrawn and utilized either through depreciation or expense after considering the usage of these funds. Since the replacement reserves are essentially the same as funded depreciation the same regulations regarding interest and equity will apply.

44.28.1 If a facility is leased from an unrelated party and the ownership of the reserve rests with the lessor, then the replacement reserve payment becomes part of the lease payment and is considered an allowable cost in the year expended. If for any reason the lessee is allowed to use this replacement reserve for the replacement of the lessee's assets then during that year the allowable lease payment will be reduced by that amount. The Lessee will be allowed to depreciate the assets purchased in this situation.

44.28.2 If a rebate of a replacement reserve is returned to the lessee for any reason, it will be treated as a reduction of the allowable lease expense in the year review.

44.29 Gains and Losses on disposal of assets. Gains and losses realized from the disposal of depreciable assets are to be included in the determination of allowable costs. The extent to which such gains and losses are includable is calculated on a proration basis recognizing the amount of depreciation charged under the program in relation to the amount of depreciation, if any, charged or assumed in a period prior to the provider's participation in the program, and in the current period.

44.29.1 The recapture will be made in cash from the seller. During the first eight years of operation, all depreciation allowed on buildings and fixed equipment by the Department will be recaptured from the seller in cash at the time of the sale. From the 9th to the 15th year all but 3% per year will be recaptured and from the 16th to the 25th year, all but 8% per year will be recaptured, not to exceed 100%. Accumulated depreciation is recaptured to the extent of the gain on the sale.

44.29.2 The buyer must demonstrate how the purchase price is allocated between depreciable and non-depreciable assets. The cost of land, building and equipment must be clearly documented. Unless there is a sales agreement specifically detailing each piece of moveable equipment, the gain on the sale will be determined by the total selling price of all moveable equipment compared to the book value at the time of the sale. No credits are allowed on moveable equipment.

44.29.3 Accumulated depreciation is recaptured to the extend of the gain on the sale. In calculating the gain on the sale the entire purchase price will be compared to net book value unless the buyer demonstrates by an independent appraisal that a specific portion of the purchase price reflects the cost of non-depreciable assets.

44.29.4 Depreciation will not be recaptured if depreciable assets are sold to a purchaser who will not use the assets for a health care service for which future Medicare, Medicaid, or State payments will be received. The purchaser must use the assets acquired within five years of the purchase. The purchaser will be liable for recapture if the purchaser violates the provisions of this rule.

44.210 Limitation on the participation of capital expenditures. Depreciation, interest, and other costs are not allowable with respect to any capital expenditure in plant and property, and equipment related to resident care, which has not been submitted to the designated planning agency as required, or has been determined to be consistent with health facility planning requirements.

44.3 Purchase, Rental, Donation and Lease of Capital Assets

44.3.1 Purchase of facilities from related individuals and/or organization where a facility, through purchase, converts from a proprietary to a nonprofit status and the buyer and seller are entities related by common and/or ownership, the purchaser's basis for depreciation shall not exceed the seller's basis under the program, less accumulated depreciation if the following requirements are met:

44.3.1.1(A) Where a facility is purchased from an individual or organization related to the purchaser by common control and/or ownership; or

44.3.1.1(B) Where a facility is purchased after April 1, 1980 by an individual related to the seller as:

- (1) a child
- (2) a grandchild
- (3) a brother or sister
- (4) a spouse of a child, grandchild, or brother or sister, or
- (5) an entity controlled by a child, grandchild, brother, sister or spouse of child, grandchild or combination brother or sister thereof; or

44.3.1.2 Accumulated depreciation of the seller under the program shall be considered as incurred by the purchaser for purposes of computing gains and applying the depreciation recapture rules Subsection 44.29 to subsequent sales by the buyer. There will be no recapture of depreciation from the seller on a sale between stipulated related parties since no set-up in the basis of depreciable assets is permitted to the buyer.

44.3.1.3 One-time exception to subsection 44.3.1.2 At the election of the seller, subsection 44.3.1.1 will not apply to a sale made to a buyer defined in subsection 44.3.1.2 if:

(a) the seller is an individual or any entity owned or controlled by individuals or related individuals who were selling assets to a "related party" as defined in subsection 44.3.1.1 or 44.3.1.2, and

(b) the seller has attained the age of 55 before the date of such sale or exchange; and

(c) during the twenty-year period ending on the day of the sale, the seller has owned and operated the facility for periods aggregating ten years or more; and

(d) the seller has inherited the facility as property of a deceased spouse to satisfy the holding requirements under subsection 44.3.1.3c

(e) if the seller makes a valid election to be exempted from the application of 44.3.1.2 the allowable basis of depreciable assets for reimbursement of interest and depreciation expense to the buyer will be determined in accordance with the historical cost as though the parties were not related. This transaction is subject to depreciation recapture if there is a gain on the sale.

44.3.1.4 The one exception to subsection 44.3.1.2 applies to individual owners and not to each facility. If an individual owns more than one facility he must make the election as to which facility he wished to apply this exception to.

44.3.1.5 Limitation in the application of subsection 44.3.1.3

44.3.1.5.1 Subsection 44.3.1.3 shall not apply to any sale or exchange by the seller if an election by the seller under subsection 44.3.1.3 with respect to any other sale or exchange has taken place.

44.3.1.5.2 Subsection 44.3.1.3 shall not apply to any sale or exchange by the seller unless the seller:

44.3.1.5.2.1 immediately after the sale has no interest in the nursing home (including an interest as officer, director, manager or employee) other than as a creditor, and

44.3.1.5.2.2 does not acquire any such interest within 10 years after the sale of this or any other facility and

44.3.1.5.2.3 agrees to file an agreement with the Department of Human Services to notify the Department that any acquisition as defined by the subsection 44.3.1.5.2.2 has occurred.

44.3.1.6 If subsection 44.3.1.5.2 is satisfied, subsection 44.3.1.1 and subsection 44.3.1.2 will also be satisfied.

44.3.1.7 If the seller acquires any interest defined by subsection 44.3.1.5.2.2, then pursuant to the agreement the basis will revert to what the seller's basis would be if the seller had continued to own the facility, the amounts paid by the Title XIX program for depreciation, interest and return of owner's equity from the increase in basis will be immediately recaptured, and an interest rate of nine percent per annum on recaptured moneys will be paid to the Department for sellers' use of Title XIX moneys. A credit against this, of the original amount of depreciation recapture from the seller, will be allowed, with any remaining amount of the original depreciation recapture becoming the property of the Department.

44.3.2 Basis of assets used under the program and donated to a provider. Where an asset that has been used or depreciated under the program is donated to a provider, the basis of depreciation for the asset shall be the lesser of the fair market value or the net book value of the asset in the hands of the owner last participating in the program. The net book value of the asset is defined as the depreciable basis used under the program by the asset's last participating owner less the depreciation recognized under the program.

44.3.3 Allowances for depreciation on assets financed with Federal or Public Funds. Depreciation is allowed on assets financed with Hill Burton or other Federal or Public Funds.

44.4 Leases And Operations Of Limited Partnerships

44.4.1 Information and Agreements Required for Leases. If a provider wishes to have costs associated with leases included in reimbursement:

44.4.1.1 A copy of the signed lease agreement is required.

44.4.1.2 An annual copy of the federal income tax return of the lessee will be made available to Representatives of the Department and of the U.S. Department of Health and Human Services in accordance with Section 27.

44.4.1.3 If the lease is for the use of a building and/or fixed equipment, the articles and bylaws of the corporation, trust indenture partnership agreement, or limited partnership agreement of the lessor is required.

44.4.1.4 If the lease is for the use of a building and/or fixed equipment, the annual federal income tax return of the lessor will be made available to representatives of the Department and the U.S. Department of Health and Human Services in accordance with section 27.

44.4.1.5 A copy of the mortgage or other debt instrument of the lessor will be made available to representatives of the Department and the U.S. Department of Health and Human Services. The lessor will furnish the Department of Human Services a copy of the bank computer printout sheet on the lessor's mortgage showing the monthly principle and interest payments.

44.4.1.6 The lease must be for a minimum period of 25 years if an unrelated organization is involved. If the lessor was to sell the property within the 25 year period to a nursing home operator or the lessee, the historical cost for the new owner would be determined in accordance with the definition of historical costs, and the portion of the lease payment made in lieu of straight line depreciation will be recaptured in accordance with subsection 44.29.

44.4.2 Lease Arrangements Between Individuals or Organizations Related by Common Control and/or Ownership. A provider may lease a facility from a related organization within the meaning of the Principles of Reimbursement. In such case, the rent paid to the lessor by the provider is not allowed as a cost. The provider, however, would include in its costs the costs of ownership of the facility. Generally, these would be costs of the lessor such as depreciation, interest on the mortgage, real estate taxes and other

expenses attributable to the leased facility. The effect is to treat the facility as though it were owned by the provider.

44.4.3 Leased Arrangement Between Individuals or Organizations Not Related by Common Control or Ownership. A provider may lease a facility from an unrelated organization within the meaning of the Principles of Reimbursement. The allowable cost between two unrelated organizations is the lesser of: (Sections 44.4.3.1 or 44.4.3.2).

44.4.3.1 The actual costs calculated under the assumption that the lessee and the lessor are related parties; or

44.4.3.2 The actual lease payments made by the lessee to the lessor.

44.4.3.3 The above principle applies unless the lessor refinances and reduces the cost of ownership below the cost of lease payments and the lessee remains legally obligated to make the same lease payment despite the refinancing. This limitation of the general rule shall not apply to any lease entered into, renewed, or renegotiated after January 1, 1990. If this limitation applies, the allowable cost shall be the actual lease payments made by the lessee to the lessor.

44.4.3.4 If the cost as defined in subsection 44.4.3.2 are less than the costs as defined in subsection 44.4.3.1, then the difference can be deferred to a subsequent fiscal period. If in a later fiscal period, costs as defined in section 44.4.3.2 exceed costs as defined in section 44.4.3.1, the deferred costs may begin to be amortized. Amortization will increase allowable costs up to the level of the actual lease payments for any given year. These deferred costs are not assets of the provider for purposes of calculating allowable costs of interest or return of owners equity and, except as specified, do not represent assets that a provider or creditor of a provider may claim is a monetary obligation from the Title XIX program.

44.4.3.5 A lease payment to an unrelated party for moveable furnishings and equipment is an allowable cost, but it shall be limited to the cost of ownership on vehicles only.

44.4.3.6 For facilities entering into, renewing, or renegotiating a lease on or after September 1, 1999, where the provider/lessee leases a nursing facility from an unrelated party and subsequently the lessor sells to another unrelated party, Sections 44.4.3.6(a) and (b) shall apply.

44.4.3.6(a) In cases where the original lessor sells, the lease payment and the terms of the original lease agreement, which have been prior approved by the Department, will be allowed. Should the lessee enter into, renew, extend, or renegotiate the original lease agreement, any terms of that lease agreement or payments related to it must be prior approved by the Department. Otherwise, the lesser of Principle 44.4.3.1 or 44.3.3.2 shall apply.

44.4.3.6(b) For the provider/lessee entering into, renewing, or renegotiating a lease on or after September 1, 1999, the following four (4) conditions must be met: